IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1925

No. 106

RHODE ISLAND HOSPITAL TRUST COMPANY,
Executor of George Briggs, Deceased,
Plaintiff in Error,

v.

RUFUS A. DOUGHTON, Commissioner of Revenue
of the State of North Carolina,
Defendant in Error.

BRIEF ON BEHALF OF THE DEFENDANT IN ERROR

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STATEMENT.

George Briggs, a resident of the State of Rhode Island, died October 29, 1919, leaving a last will and testament in which he appointed the plaintiff in error, Rhode Island Hospital Trust Company of Providence, Rhode Island, hereinafter called the Trust Company, his executor. The Trust Company duly qualified as executor in the municipal court of the city of Providence, Rhode Island, November 25, 1919. The estate so bequeathed was quite valuable. Of it were certain shares of stock of the R. J. Reynolds Tobacco Company, hereinafter called the Tobacco Company, the appraised value of which was $115,634.50. All of said stock was bequeathed to legatees who resided without the State of North Carolina (R. p. 22) and the shares of stock themselves were physically located out of the State of North Carolina at the time of decedent's death. The Tobacco Company was incorporated in the State of New Jersey April 4, 1899, (R. p. 26). (Note: It had also been incorporated in North Carolina February 27, 1899,

Chapter 109, Private Laws 1899. See copy of the act as Appendix A to this brief.) The Tobacco Company domesticated in North Carolina under Section 1194 of the Revisal of 1905, now Section 1181 of the Consolidated Statutes of 1919, August 14, 1906, (R. p. 27). Two-thirds in value of the Tobacco Company's entire property was located in North Carolina before and at the time of the death of Mr. Briggs and has been so located at all times since (R. p. 32). The predecessor of the present defendant in error, the Commissioner of Revenue of North Carolina, to whom had been committed the administration of the inheritance tax law applicable to this estate, Part 2 of Chapter 131, Consolidated Statutes of 1919, Second Volume, Sections 7772 *et sequitur;* Chapter 40, Public Laws 1921, assessed an inheritance tax of $2,678.85 upon the transfer of two-thirds in value of the stock of decedent in the Tobacco Company. This sum was paid by the Trust Company, plaintiff in error, to the Commissioner of Revenue of the State of North Carolina under protest and this action was brought to recover said sum so paid. There is no controversy as to the amount paid and no contention that the amount is incorrect if the statute under which it is levied is constitutional. The statute particularly involved is as follows: section 7772 *ut sup.*, p. 946 and section 7776, p. 948,

> "From and after the passage of this act all real and personal property of whatever kind and nature which shall pass by will or by the intestate laws of this State from any person who may die seized or possessed of the same while a resident of this State, whether the person or persons dying seized thereof be domiciled within or out of the State (or if the decedent was not a resident of this State at the time of his death, such property or any part thereof within this State), or any interest therein or income therefrom which shall be transferred by deed, grant, sale, or gift, made in contemplation of the death of the grantor, bargainor, donor, or assignor, or intended to take effect in possession or enjoyment after such death, to any person or persons or to bodies corporate or politic, in trust or otherwise, or by reason whereof any person or body corporate or politic shall become beneficially entitled in possession or expectancy to any property or the income thereof, shall be and hereby is made subject to a tax for the benefit of the State as follows, that is to say:
>
> . . . . .

"Seventh. The words 'such property or any part thereof or interests therein within this State' shall include in its meaning bonds and shares of stock in any incorporated company, incorporated in any other state or country, when such incorporated company is the owner of property in this State, and if 50 per cent or more of its property is located in this State, and when bonds or shares of stock in any such company not incorporated in this State, and owning property in this State, are transferred by inheritance, the valuation upon which the tax shall be computed shall be the proportion of the total value of such bonds or shares which the property owned by such company in this State bears to the total property owned by such company, and the exemptions allowed shall be the proportion of exemption allowed by this act, as related to the total value of the property of the decedent.

"Any incorporated company not incorporated in this State and owning property in this State which shall transfer on its books the bonds or shares of stock of any decedent holder of shares of stock in such company exceeding in par value five hundred dollars, before the inheritance tax, if any, has been paid, shall become liable for the payment of the said tax, and any property held by such company in this State shall be subject to execution to satisfy same. A receipt or waiver signed by the State Tax Commission of North Carolina shall be full protection for any such company in the transfer of any such stock or bonds."

The Supreme Court of North Carolina interpreted this statute as requiring the assessment and collection of this tax. The Court further held that, so interpreted, it did not offend against either the State or Federal Constitution. See R. pp. 40 to 50, inclusive; 187 N. C., 263.

The Federal question involved in the determination of this cause, then, arises out of the alleged opposition of this statute so interpreted to Section 1 of the Fourteenth Amendment to the United States Constitution. The Trust Company, plaintiff in error, contends that shares of stock in a corporation are themselves property whose situs is the domicile of their owner, regardless of the location of the property of the corporation without which the shares could have no value. This contention is necessarily based upon the theory that such shares of stock are property in the hands of their owner by a fixed, rigid and invariable rule of law, and, being such, the State cannot tax their transfer in the instant

case without contravening the due process of law or equal protection provision of the Fourteenth Amendment.

The defendant in error controverts this contention. He says that the conception of a corporation as an entity apart from its shareholders is a mere fiction of law, valuable in defining its duties and responsibilities as a corporate body to the public and to its members. Otherwise, it may be disregarded by the Legislature for the real truth and substance of the thing without such Legislature being guilty of extortion or of offending against due process. In the instant case the shares of stock involved are in reality engraved paper having no intrinsic value. They are valuable only because they are evidence of an aliquot interest in property, two-thirds of which is located in North Carolina. The General Assembly of North Carolina by express legislation has adopted this theory and so in no sense can the law quoted above offend against the Fourteenth Amendment. Particularly is this true when this legislation did not arise out of the fact itself, but was merely an extension to inheritance taxes of the general policy of the State shown for forty years or more in its taxation of corporations and of the shares of stock of such corporations in the hands of individual holders.

SUMMARY OF POINTS ARGUED.

(1) An inheritance tax is in no sense a tax upon property, but is a levy upon the exercise of a state granted privilege to dispose of property at one's death or to receive such property by reason of the death of the former holder.

(2) The authority to tax this privilege is not restricted by the Fourteenth Amendment unless the statute plainly offends against the due process or equal protection clauses of that Amendment.

(3) The idea of a corporation as a legal entity, or person apart from its members, is a mere fiction of law. When this fiction is urged to an extent not within its reason and purpose, it should be disregarded and the corporation considered as an aggregation of persons both in equity and law.

(4) The State of North Carolina adopted this rule years ago and has adhered to it consistently since in raising revenue by taxa-

tion of property of corporations and of the shareholders in such corporations. The act of 1919, set out in full above, but extended this salutary and just principle to inheritance taxes.

(5) The act thus interpreted does not offend against the Fourteenth Amendment as the shares of stock held by the decedent in another state are not themselves property but only evidences of his ownership of an interest in property actually located in North Carolina, the statute being careful to fit the taxable value of the transfer of such shares to the proportion of the property owned and operated by the corporation within the State.

(6) As this is in reality taxation of the transfer of an interest in property located in the State, the General Assembly may impose the obligation to pay such tax upon the custodian of the property within the State. Much more may it, then, impose this liability upon the Tobacco Company in the instant case if it should transfer the stock of decedent upon its books without the waiver of the Commissioner of Revenue required to give such transfer validity.

ARGUMENT.

I.

An inheritance tax is in no sense a tax upon property but is a levy upon the exercise of a State granted privilege to dispose of property at one's death or to receive such property by reason of the death of the former holder.

The authorities are so uniform to the effect thus stated that it is not necessary to cite many cases.

IN NORTH CAROLINA:

> "We do not regard the tax in question as a tax on property, but rather as a tax imposed on the succession—on the right of the legatee to take under the will or of a collateral distribution in the case of intestacy. . . . Neither can it be held a tax on property merely because the amount of the tax is measured by the value of the property."

Pullen v. Commissioners, 66 N. C., 363.

"A succession tax is a tax on the right of succession to property and not on the property itself. The right to take property by devise or descent is not one of the natural rights of man, but is the creature of the law."

In re Morris' Estate, 138 N. C., 259;
State v. Bridgers, 161 N. C., 247;
Norris v. Durfey, 168 N. C., 321;
In re Inheritance Tax, 168 N. C., 356;
Corp. Com. v. Dunn, 174 N. C., 679;
Wach. B. & T. Co. v. Doughton, 189 N. C., 50.

IN THE UNITED STATES COURT:

"An inheritance tax is not one on property but one on the succession. The right to take property by devise or descent is the creature of the law and not a natural right; a privilege, and therefore, the authority which confers it may impose conditions upon it."

Magoun v. Bank, 170 U. S., 283;
Knowlton v. Moore, 178 U. S., 41;
Blackstone v. Miller, 188 U. S., 207;
Chandler v. Kelsey, 205 U. S., 466;
Keeney v. New York, 222 U. S., 525;
Wheeler v. Sohmer, 233 U. S., 434;
Bullen v. Wisconsin, 240 U. S., 625;
Maxwell v. Bugbee, 250 U. S., 525;
Watson v. State Comptroller, 254 U. S., 122;
Nickel v. Cole, 256 U. S., 222.

II.

The authority to tax this privilege is not restricted by the Fourteenth Amendment unless the statute plainly offends against the due process or equal protection clause of that amendment.

"It is true that this case (*Carpenter v. Pennsylvania* 17 How., 456) was decided before the adoption of the 14th Amendment, but we think it correctly defines the limits of jurisdiction between the State and Federal Governments, in respect to the control of the estates of decedents, both as they were regarded before, and have been regarded since, the adoption of the 14th Amendment. It has never been held that it was the purpose or function of that amendment to change the systems and policies of the states in regard to

the devolution of estates, or to the extent of their taxing power over them." *Orr v. Gilman*, 183 U. S., 278.

"And, excluding our right to consider policies or assume legislation, we have many times said that a state in its purposes and in the execution of them must be allowed a wide range of discretion, and that the court will not make itself a harbor in which can be found a refuge from ill-advised, unequal and oppressive legislation. 102 U. S., 691." *Billings v. Illinois*, 188 U. S., 97.

"The 14th Amendment does not deprive a state of the power to regulate and burden the right to inherit, but at the most can only be held to restrain such an exercise of power as would exclude the conception of judgment and discretion, and which would be so obviously arbitrary and unreasonable as to be beyond the pale of governmental authority." *Campbell v. California*, 200 U. S., 87. See, also,

Cahen v. Brewster, 203 U. S., 543;
Board of Education v. Illinois, 203 U. S., 553;
Beers v. Glynn, 211 U. S., 477;
Moffit v. Kelly, 218 U. S., 400;
Stebbins v. Riley, No. 227, Oct. Term, 1924, 45 S. C., Rep. 424.

III.

The idea of a corporation as a legal entity or person apart from its members is a mere fiction of law. When this fiction is urged to an extent not within its reason and purpose it should be disregarded and the corporation considered as an aggregation of persons both in equity and law.

The words "association of persons," are often, and not inaptly, employed to describe a corporation. An incorporated company is an association of individuals acting as a single person, and by their corporate name. As this Court has said "private corporations are but associations of individuals united for some common purpose, and permitted by law to use a common seal, and to change its members without a dissolution of the corporation." *Baltimore & P. R. Co. v. Fifth Baptist Church*, 108 U. S., 317; *United States v. Trinidad Coal & C. Co.*, 137 U. S., 160. See, also, *Hale v. Henkel*, 201 U. S., 43.

"Undoubtedly a corporation is, in law, a person or entity entirely distinct from its stockholders and officers. . . . But while this presumption should be enforced to protect the corporation, it should not be carried so far as to enable the corporation to become a means of fraud, *or a means to evade its responsibilities.*" *J. J. McCaskill Co. v. United States,* 216 U. S., 504. See, also, *Linn Timber Co. v. United States,* 236 U. S., 574; *Northern Securities Co. v. United States,* 193 U. S., 332; *Standard Oil Co. v. United States,* 221 U. S., 1; *United States v. American Tobacco Co.,* 221 U. S., 106.

It will, however, be said that in each of these cases the corporate fiction was set up as a shield for a positive wrong, and the courts disregarded it for that reason. "Fictions of law, invented to promote justice, can never be invoked to accomplish its defeat." *Mostyn v. Fabrigas,* Cowp., 177. This, we submit, is but to say that the fiction was made by judges, and so may be disregarded by them, when in the administration of the law it should run counter to their conception of justice. The proper law-making power in this country, though, is the legislature, and it cannot be successfully controverted that it has authority to modify, or abolish fictions, though they may have been judicially created. We will return to this in the discussion under the subhead V.

IV.

The State of North Carolina adopted this rule years ago and has adhered to it consistently since in raising revenue by the taxing of corporations and of the shareholders in such corporations. The Act of 1919, set out in full above, but extended this salutary principle to inheritance taxes.

Chapter 117, sec. 8 (6), Laws 1881 provided:

"Stockholders in valuing their shares" (for taxation) "may deduct their ratable proportion of the value of taxable property, the tax whereof is paid by the corporation."

Chapter 363, sec. 8, Laws 1883, brings the same provision forward, as does chapter 177, sec. 12 (6), Laws 1885.

See *Railroad Co. v. Commissioners,* 87 N. C., 414.
Worth v. Railroad, 89 N. C., 301.
Railroad Co. v. Commissioners, 91 N. C., 454.

The remaining acts herein referred to are substantially similar.

Chapter 137, sec. 14, Laws 1887;
Chapter 218, sec. 16, Laws 1889;
Chapter 326, sec. 15, Laws 1891;
Chapter 296, sec. 14, Laws 1893;
Chapter 119, sec. 14, Laws 1895;
Chapter 169, sec. 14, Laws 1897;
Chapter 15, sec. 14, Laws 1899;
Chapter 9, sec. 9, Laws 1901;
Chapter 247, sec. 4, Laws 1903;
Chapter 588, sec. 4, Laws 1905;
Chapter 256, sec. 4, Laws 1907;
Chapter 438, sec. 4, Laws 1909;
Chapter 46, sec. 4, Laws 1911;
Chapter 201, sec. 4, Laws 1913;
Chapter 285, sec. 4, Laws 1915;
Chapter 231, sec. 4, Laws 1917;
Chapter 90, sec. 4, Laws 1919.

From 1887 to 1899 the method set out in the statutes was as follows:

"Persons owning shares in incorporated companies, taxable by law, are not required to deliver to the list taker a list thereof, but the president or chief officer of such corporation shall deliver to the list taker a list of all shares of stock held therein and the value thereof, except banks. The tax assessed on shares of stock embraced in said list shall be paid by the corporations respectively. *Provided*, that (this) section cannot be construed so as to impose a double tax on said corporation."

The effect of this was, of course, to tax the property of the corporation and exempt wholly its shares in the hands of its shareholders from taxation, there being in the statute no authority given the corporation to charge this stock tax to its several shareholders.

From 1901 to 1919 inclusive the statutes were more direct:

"Individual stockholders in any corporation, joint stock association, limited partnership or company paying a tax on its capital stock, shall not be required to pay any tax on said stock or to list the same."

The stock tax referred to above was, under the Act of 1919, section 7771 of the Consolidated Statutes of 1919, a single state tax amounting to thirty-six cents on the $100 of value of such

stock, ascertained in the manner provided in section 7941 of the same compilation. There were so many deductions allowed in estimating the value of this stock, that in 1919, out of a capitalization of domestic corporations, excluding public service corporations and banks, of $160,000,000, approximate, the net proceeds of this tax was $347,055.06, as shown by the report of the State Treasurer, 1919-1920, page 34.

In 1915 this privilege of exemption of shares of stock from taxation was extended to corporations holding shares in other corporations. Section 4, chap. 285. In 1917, section 4, chap. 231, this was added to section 4: "Nor shall any individual stockholder of any foreign corporation be required to list or pay taxes on any share of its capital stock, if two-thirds in value of its entire property is situated and taxed in the State of North Carolina, and the said corporation pays franchise tax on its entire issued and outstanding capital stock at the same rate as paid by domestic corporations."

By the act of 1919, chapter 90, sec. 4, another alternative was incorporated in this clause: "or if such corporation has tangible assets in this State assessed for taxation at a value exceeding the par value of the total stock owned by citizens of this State," see section 7771 of Consolidated Statutes 1919.

The Tobacco Company availed itself of these provisions. Record p. 30.

As further showing that the fiscal and economic policy of the State identified the property of the shareholder in his share with that of the corporation in its property, attention is called to the fact that in 1921 the State ceased levying any stock tax upon the corporation, yet maintained in active force the exemption of such shares of stock in the hands of the shareholder from any taxation. P. L. 1921, chapter 34, sections 3 and 4. Again, in 1923, P. L. 1923, chapter 4, sec. 4, the General Assembly to avoid double taxation, put shares of stock in a foreign corporation on the same footing as shares in a domestic corporation as to exemption from taxation, using the following words: "Nor shall any individual stockholder of any foreign corporation be required to list or pay taxes on any share of its capital stock in this State, and the situs of such shares of stock in foreign corporations, owned by residents of this State for the purpose of this act is hereby declared to be

at the place where such corporation undertakes and carries on its principal business."

This exemption of shares of stock in domestic corporations from taxation was challenged in *Person v. Watts*, 184 N. C., 499, as offending against section 3 of Article V of the State Constitution. That section, so far as material is:

"Laws shall be passed taxing, by a uniform rule, all moneys, credits, investments in bonds, stocks, joint stock companies, or otherwise; and also all real and personal property, according to its true value in money."

The Court, however, sustained the constitutional validity of the exemption in an exhaustive opinion in which the subject is treated fully, both in its historical and in its legal and constitutional aspects.

At page 508, *Adams, J.*, says: "Certainly there can be no doubt that the shareholder's 'investment' is taxed as the Constitution requires. The truth is, the certificate of stock represents the shareholder's investment in the corporation as the landholder's deed represents his investment in the land. If the land is taxed why tax the deed? If the capital stock is taxed, why tax the certificate which represents the stock? No doubt the Legislature possesses the power to repeal the statute and to tax both; no doubt it possesses the power to devise a system of taxation that would be more burdensome to all classes, but if the Constitution does not require it, why should such additional burden be imposed? It is not denied that shares of stock in a restricted sense are the individual property of the owner, and in such sense may be considered as separate from the capital stock. The holder may sell his certificate without the consent of the company, but in doing so he sells only his interest in the corporation. His interest as a shareholder may become adverse to that of the corporation, but by investing in the capital stock he parts with the individual control of his money. It is only in this limited sense that shares of stock are separate from the corporation. In its broader and more real sense the interest of the shareholder is inseparable from that of the corporation. In the larger sense there is but one property, for shares of stock have value only as the taxed property of the corporation has value. During his lifetime the owner can derive no income from his shares unless the business of the corporation

earns a profit; *and upon his death, when his personal property passes to his distributees, it is not the certificate that is subject to an inheritance tax, but under a special act the value of the owner's interest in the corporation represented by the certificate, just as such tax is assessed, not upon the deed, but upon the value of land which descends from the ancestor to the heir.*"

The Supreme Court of North Carolina reaffirms this position in *Person v. Doughton*, 186 N. C., 723. In the decision in that case it was dealing with the act of 1923, which exempted shares of stock in foreign corporations from taxation.

It is therefore, we submit, demonstrated that for years both the legislative and judicial departments of the State have disregarded the fiction of a separate corporate entity, as a matter of public policy, in all revenue legislation, and that the act of 1919, was intended to co-ordinate the inheritance tax law with the other revenue acts of the State.

V.

The Act thus interpreted does not offend against the Fourteenth Amendment as the shares of stock held by the decedent in another State are not themselves property, but only evidence of decedent's ownership of an interest in property actually located in North Carolina, the statute being careful to fit the taxable value of the transfer of such shares to the proportion of the property owned and operated by the corporation in the State.

This is true:

First, because while title to corporate property is in the corporation, the substantial beneficial ownership is, in equity at least, in the stockholders. Stockholders acting as a body unanimously, may execute a valid mortgage on the corporate property.

> *Gadsden First National Bank v. Winchester*, 119 Ala., 168;
> *Swift v. Smith*, 65 Md., 428;
> *Bundy v. Ophir Iron Co.*, 38 Oh. St., 300.

The beneficial interest is in the stockholders.

> *United States v. Wolters*, 46 Fed., 509;
> *Warren v. Davenport Fire Ins. Co.*, 31 Iowa, 464;
> *State v. Brinkhop*, 238 Mo., 298.

This interest is insurable.

Seaman v. Enterprise F. & M. Ins. Co., 21 Fed., 778;
Aetna Fire Ins. Co. v. Kennedy, 161 Ala., 600;
Riggs v. Commercial Mut. Ins. Co., 125 N. Y., 7.

Many of the cases in this Court, which recognize a distinct property in the shareholder in his shares of stock, do so in determining the constitutionality of a statute, which was enacted in recognition of this principle. See *Hawley v. Malden*, 232 U. S., 1. In truth, then, they simply sustain statutes which make the corporate fiction a reality, and should be, we submit, interpreted in this light. Why, then, are they not authorities for the position taken in this brief:—that the Legislature may, without conflict with the 14th Amendment, disregard this fiction for the reality of the matter? Compare *Blackstone v. Miller*, 188 U. S., 189, with *Wheeler v. Sohmer*, 233 U. S., 434.

In *Denver v. Hobbs' Estate*, 144 Pac. Rep., 874, 58 Colo., 220 it is said:

> "It is urged that shares of stock in a foreign corporation are the personal property of the owner, separate and distinct from the capital of the corporation, for which reason they form separate and distinct subjects for taxation and should be thus taxed at the residence of the owner. Assuming they are personal property, they are inconsequential property. They are merely tokens or evidence of ownership of an interest in corporate property of a corporation or something of the kind unnecessary to determine and if destroyed, the holder loses nothing. He is still the owner of what they purported to represent. It is of that class of property that its situs for the purpose of taxation is a matter of legislative control, as is also the method to be provided by its assessment."

See *Tappan v. Merchants National Bank*, 86 U. S., 490; *Farrington v. Tenn.*, 95 U. S., 679; *Corry v. Baltimore*, 196 U. S., 466; *Rogers v. Hennipen County*, 240 U. S., 184.

Chief Justice Chase dissented in *Van Allen v. The Assessors*, 70 U. S., 598, but this part of his dissenting opinion was not in conflict with the opinion of the Court:

> "It is true that the shareholder has no right to the possession of any part of the corporate property while the corpora-

tion exists and its affairs are honestly managed. He has committed his interest, for a time, to the possession and control of the corporation of which he is a member, and he has only a member's voice in the management of it.

"So a man who has leased a farm has no right to possession or control during the lease; but who denies his property in the farm? And if a dozen owners join in the lease, has not each one an interest in the property to the extent of one-twelfth?

"So, if for the time the property of the shareholder is placed beyond his direct control and converted into property of the association, how can that circumstance affect the intrinsic character of his shares as shares of the whole corporate property? How can a man's shares of any property be subject of valuation at all if not with reference to the amount and productiveness of the property of which they are a part? What value can they have except that given them by that amount and that productiveness? A certificate of title to a share is not a share. It is evidence of the shareholder's interest. His interest may be transferred by the transfer of the certificate; but it is not the certificate that is valued when the worth of the share is estimated either by the speculator in the market or by the tax assessor. It is the property which it represents that is valued by the speculator, often with reference to speculation only, but by the public officer, always, if he does his duty, by the real worth of the property, all things considered."

In I Morawetz on Corporations, 2d Edition, section 227, p. 221 it is said:

"The statement that a corporation is an official person or entity apart from its members is merely a description in figurative language of a corporation viewed as a collective body. A corporation is really an association of persons and no judicial dictum or legislative enactment can alter this fact."

Section 232 idem. p. 227.

"In all cases it is indispensable that the fiction of a corporate entity apart from the individual shareholders be preserved unimpaired in measuring and enforcing those rights and obligations *which are of a corporate character.*"

See, also, 3 Cook on Corporations, 8th Edition, sections 663 and 664.

It is stated in section 27 (subsection 7) of 14 C. J., p. 63:

> "While the title and ownership of property and business of a private business corporation is vested in the corporation as a distinct legal entity and artificial person, the stockholders or members are nevertheless interested therein within the meaning of the statutes and rules of law since the beneficial interest is in them."

The basis of the rule making a corporation a distinct entity and the modifications of that rule are thus stated in section 20 (subsection 4) of 14 C. J., p. 59:

> "Although the doctrine that a corporation is a legal entity and person in the law distinct from the members who compose it will always be recognized and given effect, both at law and in equity, in cases which are within its reason and when there is no controlling reason against it, and although in some cases it seems to have been given effect contrary to reason, it is clear that a corporation is in fact a collection of individuals who, in the case of modern private corporations, really own its property and carry on the corporate business, through the corporation and its officers and agents, for their own profit or benefit, and that the idea of the corporation as a legal entity or person apart from its members is a mere fiction of the law introduced for convenience in conducting the business in this privileged way; and it is now well settled, as a general doctrine, that, when this fiction is urged to an intent not within its reason and purpose, it should be disregarded and the corporation considered as an aggregation of persons, both in equity and at law."

Second. The State has constitutional authority to disregard this fiction, particularly when this is done with no ulterior purpose but with the intent to conform its inheritance tax laws to its consistent policy of disregarding the fiction in all of its revenue acts in relation to the taxation of the property of corporations and of their shareholders. It is declared in *Blackstone v. Miller,* 188 U. S., 189:

> "When logic and the policy of a state conflict with a fiction due to historical tradition, the fiction must give way."

See *Adams Express Company v. Ohio State Auditor*, 166 U. S., 185; *New Orleans v. Stemple*, 175 U. S., 309. There is nothing, we submit, in the recent case of *Frick v. Pa.*, Nos. 122 to 125, October Term of this Court, 45 S. C. Rep., 603, which conflicts with this view. The effect of that decision was to deny the State authority to assess a transfer or inheritance tax upon tangible personal property located without its boundaries. In this case, while it is true that the Tobacco Company is technically a corporation organized under the laws of New Jersey, yet its real habitat, in the sense in which it does most the larger proportion of its business, is in the State of North Carolina where it has domesticated and in which it does an enormous business. At p. 29 of the Record is a statement of the authorized capital stock of the company, of its par value and of the amount issued and paid for. Its principal place of business is in the State of North Carolina and it has not only, as above said, domesticated in the State, but it has submitted itself to its jurisdiction under section 4 of the Revenue Act of 1919 hereinbefore set out in full (R. p. 28). It is contended that under such circumstances the State has constitutional authority to levy an inheritance tax upon the transfer of only that part of the stock which is represented by the value of the property located in the State. This is fair and just, because the Tobacco Company is conducting its very profitable business under the fostering care of the laws of the State of North Carolina and practically all the profits that accrued to the decedent during his life from his ownership of his shares of stock in this corporation accrued in the State of North Carolina. See *Young v. South Tredegar Iron Company*, 85 Tenn., 189; *In re Bronson's Estate*, 150 N. Y., 44, and *In re Culver's Estate*, 145 Iowa, 1. In *Young v. South Tredegar Iron Company*, the corporation was in the State of Tennessee in very much the same manner as the Tobacco Company is now in the State of North Carolina. Under the statutes of Tennessee an attachment was levied upon the interest of a non-resident shareholder in that corporation in Tennessee and such levy was sustained. See, also, *Parks Cramer Company v. Southern Express Company*, 185 N. C., 428.

If the position contended for is not sound, then it is easy to conceive a corporation incorporated in another state and doing business in this State with all of its property in the State, whose

shares of stock would not be and could not be subject to the inheritance tax levied by the State. We submit that under such circumstances the Courts will be permitting an injustice to be done to the citizens of the State of North Carolina in denying the right of the Legislature to disregard the fiction of a corporate entity. As hereinbefore said, this fiction is uniformly disregarded by the Courts whenever in the opinion of the Court it would work an injustice. Here, then, is the State of North Carolina which has put in effect a State policy in relation to its taxation and has followed that policy for many years in which this fiction of corporate entity has been uniformly disregarded, and now it has in express terms applied this public policy in this particular to inheritance taxes, not with the view so much to impose this tax upon such a class of transfer as to conform its inheritance tax law to its declared policy. It seems certain, we submit, that if Courts may disregard the corporate fiction to meet their conception of public policy and the right of things, much more may the Legislature disregard such fiction.

VI.

As this is in reality taxation of the transfer of an interest in property located in the State, the General Assembly may impose the obligation to pay such tax upon the custodian of the property within the State. Much more may it, then, impose this liability upon the Tobacco Company in the instant case if it should transfer the stock of decedent upon its books without the waiver of the Commissioner of Revenue required to give such transfer validity.

A state can under its taxing power and without denial of due process, tax property having a situs within its borders, irrespective of the residence of the owner and can impose, if necessary, the obligation to pay such tax upon the custodian or possessor of such property.

Kirkland v. Hotchkiss, 100 U. S., 498;
Bristol v. Washington Co., 166 U. S., 141;
Carstairs v. Cochran, 193 U. S., 10.

Chief Justice Fuller in *Bristol v. Washington Co., supra*, quotes with approval the following extract from the opinion of the Supreme Court of Minnesota in 35 Minn., 215:

> "The obligation to pay taxes on property for the support of the government arises from the fact that it is under the protection of the government. Now, here was property within this State, not for a mere temporary purpose, but as permanently as though the owner resided here. It was employed here as a business by one who exercised over it the same control and management as over his own property, except that he did it in the name of an absent principal. It was exclusively under the protection of the laws of this State. It had to rely on those laws for the force and validity of the contracts on the loans, and the preservation and enforcement of the securities. The laws of New York never operated on it. If credits can ever have an actual situs other than the domicil of the owner, can ever be regarded as property within any other state, and as under obligation to contribute to its support in consideration of being under its protection, it must be so in this case."

Justice Brewer in *Carstairs v. Cochran, supra*, declares:

> "A state has the undoubted power to tax private property having a situs within its territorial limits; and may require the party in possession of the property to pay the taxes thereon."

See, also, *Travis v. Yale & Towne Mfg. Co.*, 252 U. S., 60. It is to be observed that the Tobacco Company is not complaining in this proceeding against the effect of this law upon it. Indeed, it could not, it having not only domesticated itself within the State, but having submitted itself to its jurisdiction for taxing purposes under the act of 1919, as hereinbefore stated. In *Travis v. Yale & Towne Mfg. Co., supra*, it is held:

> "A state may, without violating the due process provision of the Fourteenth Amendment, impose a tax on the incomes of nonresidents arising from any business, trade, profession, or occupation carried on within its borders, enforcing payment, so far as it can by exercise of a just control over persons and property within the state, as by garnishment of credits."

Plaintiff in error relies upon certain cases which deal with the taxation of the transfer by a non-resident decedent of shares of stock in a corporation chartered in another state but located with part of its property in the state proposing to collect the tax. These cases naturally fall into two classes:

(a) Those where the court in interpreting a general statute, which does not specifically impose a tax, holds that the tax cannot be assessed under the general words of the act in question because the property in the share of stock is distinct from the property of the corporation itself, and the share being located without the taxing state, it has no authority to impose the tax.

People v. Bennett, 276 Ill., 43;
People v. Blair, 276 Ill., 623;
State v. Dunlap, 28 Idaho, 784;
Welch v. Burrell, State Treas., 223 Mass., 87;
In re Harkness Estate, 83 Okla., 107.

It is manifest, we respectfully submit, that these cases are in no way conclusive here,—indeed, they are scarcely in point, for in none of the statutes involved had the state acted by positive legislation upon the corporate fiction. In other words, these decisions did not determine the constitutional power of the state. They interpreted the particular act as not conferring upon the taxing authority of the particular state the power claimed. There can be no doubt that the North Carolina court, in the cause herein reviewed, would have adopted the principle of these cases had not the statute of that State created a new and different situation. See opinion, Record pp. 40 to 53, particularly at 41. The whole *ratio decidendi* is based upon this manifest distinction.

(b) Those which hold an act somewhat similar to the North Carolina act attacked herein, unconstitutional. The Wisconsin Act, 1 Wisconsin Statutes, p. 800, was as follows:

> "Sec. 72.11 (3): Where stocks, bonds, mortgages or other securities of corporations organized under the laws of this State or of foreign corporations owning property or doing business in this State shall have been transferred by a non-resident decedent, the tax shall be upon such proportion of the value thereof as the property of such corporation in this

> State bears to the total property of the corporation issuing such stocks, bonds, mortgages, or other securities."

Luse, District Judge, held this act unconstitutional in *Tyler v. Dane County,* 289 Fed., 843, and this decision was followed by the Supreme Court of Wisconsin in *Shepard v. The State,* 184 Wis., 88. Both of these decisions were founded upon the principle that in Wisconsin there is a fundamental difference between the capital of a corporation and its capital stock. The former belongs to the corporation; the latter, when issued, to the stockholder. Thus *Judge Luse* says, *Tyler v. Dane County, supra,* at p. 851:

> "By section 1751 of the Wisconsin Statutes it is provided that 'the capital stock of every corporation divided into shares, shall be deemed personal property,' and by the Uniform Stock Transfer Act adopted in 1913 the idea of the independence of the shares as property, distinct from that of the corporation, is accentuated by provisions permitting transfer by delivery of the certificate, indorsed in blank, notwithstanding charter or other formerly equally binding regulations requiring transfer on the books of the corporation."

This, of course, is a statutory definition of the relation of the stockholder to the corporation of which he is a member, as is shown by the context of the act cited. North Carolina has an act somewhat similar: section 1164 of the Consolidated Statutes of 1919, Volume I, page 500:

> "*Transfer of shares.* The shares of stock in a corporation are personal property, and are transferable on the books of the corporation in the manner and under the regulations provided by the by-laws. Whenever a transfer is made for collateral security, and not absolutely, it shall be so expressed in the entry of the transfer."

This was first enacted in 1901, section 21 of chapter 2, Laws of 1901, the chapter being entitled "An act to revise the corporation law of North Carolina." This simply defines the relation of the stockholder to the corporation. See *Bleakley v. Candler,* 169 N. C., 16. Before, at the time of, and subsequent to, its enactment, the State of North Carolina for all the purposes of taxation

has treated a share of stock as representing an interest in the corporation, as we think we have shown heretofore in this brief. In Wisconsin, however, the share of the stockholder in a corporation is not exempt from taxation on account of his relation to that corporation, which itself pays taxes on its property. It is absolutely exempt with all other property of a similar nature. That statute is as follows:

> "All moneys or debts due or to become due to any person and all stocks and bonds, including bonds issued by any county, town, city, village, school district or other political sub-division of this State not otherwise specially provided for."

Wisconsin Statutes, Volume I, section 70.11, p. 762.

This difference in the situation in Wisconsin and that in North Carolina creates a distinction between those cases and this, which is to some extent, at any rate, fundamental. The question here is, does the Fourteenth Amendment prohibit the State of North Carolina from extending to inheritance taxes its general policy as shown for many years in its identification of property in the share of stock with the property of the corporation itself for all taxation purposes?

There is another case, determined by the Supreme Court of Montana, *State ex rel. Trust Co. v. Walker*, 70 Mont., 484, which is somewhat nondescript. It quotes the Montana statute, states that it was adapted from the Wisconsin law, and holds that it was not the intention of the Legislature under that statute to submit shares of stock of the same description, character and location as those in the instant case to an inheritance tax. This case, then, cannot be considered as persuasive on this hearing.

We respectfully submit that the statute here attacked is valid and constitutional, and that the judgment of the Supreme Court of North Carolina should be in all respects affirmed.

DENNIS G. BRUMMITT,
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FRANK NASH,
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of North Carolina,
For Defendant in Error.

EXHIBIT "A"

Chapter 109, Private Laws of North Carolina, 1899.

AN ACT TO INCORPORATE THE R. J. REYNOLDS TOBACCO COMPANY.

The General Assembly of North Carolina do enact:

Section 1. Richard J. Reynolds, William N. Reynolds, Walter R. Reynolds and Robert C. Critz, of Winston, North Carolina, and John F. Parlett, of Baltimore, Maryland, their successors and assigns, are hereby created a body politic and corporate under the name of "R. J. Reynolds Tobacco Company," with a capital stock of one million two hundred thousand dollars, with the liberty and authority to increase the same from time to time or at any one time not to exceed twelve million dollars, to be divided into shares of one hundred dollars each; said stock shall be common and preferred stock, issued in the proportion of two shares of common stock to one share of preferred stock. Said preferred stock shall entitle the holder to receive in each year a dividend to be fixed at the time of the issue of the stock, of not more than eight per centum, payable half-yearly, before any dividend shall be set apart or paid on said general or common stock, and if the net proceeds in any year shall not be sufficient to pay the dividend aforesaid on said preferred stock, that such dividend shall be paid thereon as the net profits of the year will suffice to pay. The holders of the preferred stock shall have a preference on the assets of the company, but the dividends thereon are not to be cumulative, but shall be payable each year out of the profits of that year or out of any unused surplus of subsequent years; and on payment of the preferred stock at its par value with all dividends due thereon, said preferred stock shall not further participate in the assets of the corporation and may be called in and paid as prescribed by the by-laws. Said preferred stock and the certificates therefor may be issued by the board of directors by resolution. Said corporation shall have the privilege and rights hereby specifically granted, and also those conferred upon corporations by the laws of North Carolina.

Sec. 2. That any three of the persons herein incorporated to effect the purpose of this act may open books of subscription and receive subscription to the capital stock of the company at such time and place as they may appoint, and when twenty-five per centum of the capital stock herein first authorized, to wit: One million two hundred thousand dollars shall have been subscribed and paid in, then the stockholders may organize the company. That property of every kind may be received in payment of the capital stock at such valuation as may be agreed upon between the subscriber or subscribers and said stockholders. The stockholders shall not be individually liable for debt or liabilities of the corporation.

Sec. 3. That said corporation is hereby authorized and empowered to conduct, transact and carry on in all its branches and in every manner or form the business of curing, manufacturing, buying and selling tobaccos; and said corporation may manufacture, buy, sell and deal in wares and merchandise of every kind and description; shall have the power to own, hold, lease, purchase, sell and convey real estate and all other kinds of property wherever situate, and own and conduct any business at its will and pleasure; banking, insurance and operating a railroad excepted. The company proposes to carry on its operation in all the other states and territories in the United States, and in all foreign countries and territories.

Sec. 4. That the stockholders of the said corporation shall have the power to make all rules and regulations for the government of said corporation and transaction of its business. They shall have power to elect, in such manner as the majority of the stock may prescribe, such officers as they deem necessary, prescribe their duties, compensation and term of service; and, in general, said stockholders may make such by-laws and regulations for the government and conduct of the said corporation and its business, not inconsistent with the laws of this State and the laws of the United States, as they may consider best calculated to serve their interest.

Sec. 5. As such corporation they may have a common seal, which they may break, change and alter at their pleasure.

Sec. 6. That the present corporation, known as the R. J. Reynolds Tobacco Company, chartered under the general law of North Carolina by articles of agreement duly filed in the office of the

clerk of the Superior Court of Forsyth County and doing business in Winston, North Carolina, shall have power and authority to sell, convey and transfer to a corporation formed under this act all its assets, franchise and property of every kind, and to merge itself therein. And the corporation organized under this act shall have power and authority to purchase, receive, take into possession and hold all the assets, franchise and property of every kind belonging to said existing corporation.

Sec. 7. That this act shall be in force from and after its ratification.

Ratified the 27th day of February, A. D. 1899.